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## **MEMORANDUM**

**Date:** November 16, 2005

**To:** Honorable City Council  
Mayor Kwame M. Kilpatrick

**From:** Joseph L. Harris  
Auditor General 

**Subject:** Investigation of Detroit Neighborhood Development Corporation Sales

**C:** Walter Watkins, Chief Development Officer  
Planning and Development Department

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This memorandum serves to provide this Honorable Body with a report of the results of our review of certain sales of property through the Detroit Neighborhood Development Corporation (DNDC). The City established and contracted with the DNDC, a non-profit organization, to acquire, clear titles, rehabilitate, manage, and sell properties formerly owned by two failed real estate and financing companies. To ensure appropriate oversight, City employees have served as DNDC officers since it was established.

On August 25 2005, Fox 2 News reported that Henry Hagood, then Planning and Development Department (PDD) Development Director, sold City-owned properties to longtime friends Dalton Brown, Marcellus Oree and Vershawn Oree on at least three occasions. Based on our preliminary analysis and news reports, the Office of the Auditor General (OAG) initiated an investigation of the sales of City-owned property.

The OAG reviewed the property sales involving Mr. Brown and the Orees for the period September 20, 2002 through January 7, 2005. Our review focused on property sales recorded at the Wayne County Register of Deeds. We also reviewed corporate records filed with the State of Michigan Department of Labor and Economic Growth. Based on our analysis of these sales, we expanded the scope of our audit to include properties sold through the DNDC.

During our review we identified a large number of property sales to the aforementioned individuals and/or the companies they represented. We determined that the initial seller of these properties was the Detroit Neighborhood Development Corporation (DNDC) rather than the PDD. We identified a pattern of immediate resale of these properties for what appeared to be a sizable profit. Some of the property sales prices were shielded from public record by tax valuation affidavits. The pattern of resale at higher prices raised questions as to whether the DNDC sold the properties for amounts less than market value and whether the DNDC made any effort to sell the properties to obtain the

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fairest and greatest benefit for the City. We identified the following as the major property purchasers of the DNDC property sales:

- Chayne Holding Group (Dalton Brown)
- Rayford Development and RAS Development Group (Rayford Jackson)
- New Detroit Real Estate (Mark Shows)
- Walter Turner

Dalton Brown/Chayne Holding Group and Rayford Jackson/Rayford Development and RAS Development Group subsequently sold properties purchased from the DNDC to:

- MV Holdings whose principles include Marcellus and Vershawn Oree; and
- Lantech Custom Homes whose principles include Durand Jackson and Mary Coates.

On September 15, 2005 we made our first request for the DNDC records from PDD. As of November 16, 2005 we have not been provided access to records. Therefore, we are providing your Honorable Body with the results of our analysis to the extent the data have allowed. The results of our audit of the PDD's Sale of City-owned Property will be issued under separate cover.



## FINDINGS AND RECOMMENDATIONS

### **1. Access to DNDC Records Denied**

The City's Chief Development Officer, Walter Watkins, refused to provide the Auditor General access to the records for the Detroit Neighborhood Development Corporation (DNDC), or to facilitate the Auditor General's attempt to gain access to records to document:

- \$10.7 million in funding provided by the PDD to the DNDC.
- An estimated \$4.6 million in rental and sales income generated by the DNDC.
- An estimated \$.6 million in rehab and homebuyer assistance funds provided by PDD to purchasers of the DNDC properties.

The PDD contracted with the DNDC to acquire, rehabilitate and bring up to code, clear titles, manage rental and vacant properties, and sell approximately 1,147 properties formerly owned by Rogers Investment Management Co. (RIMCO) and MCA Financial Corp. (MCA). The initial contract amount was \$5.3 million. An amendment increased the contract to \$20.3 million. The PDD paid the DNDC a total of \$10.7 million on the contract. City financial records show \$5.6 million was paid to the DNDC to acquire 1,147 RIMCO/MCA properties. The remaining \$5.1 million was paid to the DNDC for advances, rehabilitation and operating expenses.

On September 15, 2005, we provided the PDD's General Manager, Jannie Warren, with a list of DNDC documents and records needed for the investigation. She informed us that she sent the list to the City's Chief Development Officer. On September 16, 2005, we made the same request of Mr. Watkins. We have been in contact with the General Manager, the DNDC attorney, and the Chief Development Officer, but have not been provided any of the documents and records requested other than the Master Agreement and part of the April 17, 2001 Agreement nullifying the Master Agreement and providing for the sale of the RIMCO/MCA properties to the DNDC. Exhibits, which include the list of properties purchased by the DNDC, were not provided. In my opinion, the Chief Development Officer, by virtue of his refusal to cooperate with the Auditor General, is obstructing the investigation.

The lack of cooperation by the PDD to provide the records, coupled with the lack of oversight over the DNDC, raises concerns about the propriety of the transactions. We are concerned that there may have been misappropriation of funds and property, and other fraudulent activity connected with the property acquired and sold through the DNDC.

The City appointed officers to DNDC's board for oversight purposes, including the former PDD Director Henry Hagood, as Secretary/Treasurer. A PDD representative informed us that the internal controls over the DNDC were poor and the PDD's administration of the DNDC was weak. We met with the President of the DNDC, Jannie Warren, at the time of our examination, who is also a General Manager of the PDD.



We question the City's level of oversight because the DNDC President, Jannie Warren, claimed that she did not know the location of the DNDC office or where the records were. We were informed that a consultant was responsible for the DNDC and reported directly to the City's Chief Development Officer. The consultant, Sylvia Bradley, did not return our phone calls.

The PDD also provided funding to some homebuyers of DNDC property. We identified 24 mortgages provided by the PDD, totaling \$638,000. New Detroit Real Estate Management, LLC, acquired the 24 homes that were subsequently mortgaged. New Detroit Real Estate Management, LLC sold the properties to the borrowers and arranged the homebuyer assistance from the PDD. State of Michigan records indicate that Mr. Mark Shows is the resident agent for New Detroit Real Estate Management, LLC. PDD documents reflect Mr. Dalton Brown as a partner. New Detroit Real Estate Management, LLC is currently being sued for mortgage fraud. Mr. Dalton Brown is a longtime friend of Mr. Hagood, the former PDD Director, who was also the Secretary and Treasurer of the DNDC.

There are indications that fraudulent activities may have occurred through the DNDC. Allegations have been made in the media that DNDC properties were sold to friends of the former PDD Director at prices below market value. Property deeds indicate that several properties were sold to these alleged friends for a nominal sum, who sold or "flipped" (sold within 21 days of purchase) the properties at a much higher price, many on the same date they acquired them from the DNDC (see Finding 2).

A PDD representative informed us that the City initially utilized Federal Community Block Grant Funds (CDBG) to fund the DNDC, but the funding source was switched to general obligation bonds because the federal controls were too restrictive. However, the general obligation bonds were sold for the purpose of purchasing and rehabilitating the properties; therefore, the funding of operating costs was an inappropriate use of the funds.

Records we obtained from the City's financial system document that only eight of the over 1,000 properties acquired by the DNDC were rehabilitated through the DNDC, which suggests that most of the homes sold by the DNDC did not meet the City's housing code and may have contained serious hazards and violations.

Furthermore, because of the lack of access to records, we cannot determine whether City housing inspectors performed presale inspections or whether the properties sold were free of hazards and serious violations. Consequently, we cannot determine whether residents of these properties are occupying housing that did not meet City housing codes at the time of sale.

The contract with the DNDC states "The Contractor shall make available in their full and complete entirety, all books, documents, ledgers, journals, papers, records (herein collectively called "Records") and project sites directly pertinent to this Agreement for monitoring, audits, inspections, examinations and making excerpts and transcriptions by the City, the federal grantor agency, and the Comptroller General of the United States, as applicable, at all reasonable times."



## **2. Questionable Disposition of DNDC Properties**

The DNDC decided, in 2002, to expeditiously dispose of its houses rather than to comply with the contract with the PDD, which required the DNDC to either rehabilitate the houses or to demolish those unsuitable for rehabilitation. The lack of a revenue source to fund the DNDC's operations was cited as a major reason.

We noted sales of 373 (32.5%) of the properties to four businessmen, during the period September 20, 2002 to January 7, 2005. 264 of these homes were resold for over \$5.8 million. However, neither Mr. Watkins nor Ms. Warren would provide us access to the DNDC records to allow us to determine the amount DNDC received for the sales and whether the sales were proper.

The PDD contract with the DNDC states "The overall objectives as to all project properties are to manage effectively and stabilize the affected real estate assets, return those properties to the general market in an orderly fashion, demolish those which are evaluated as unsuited to rehabilitation and promote comprehensive redevelopment of neighborhood blocks and communities."

Per the contract scope of services, funds provided pursuant to the contract may be used by the DNDC for the following:

1. Acquisition of properties;
2. Rehabilitation, demolition, management and maintenance of the properties to protect current tenants and to preserve neighborhoods;
3. Sale of the properties to current residents or others; and
4. Relocation costs when necessary due to sale, rehabilitation or HUD regulation.

The DNDC failed to rehabilitate the RIMCO/MCA properties it acquired with City provided funds. The City's financial records show only eight properties were rehabilitated at a total cost of \$295,932. The contract provided for \$9.6 million to rehabilitate the properties. It was expected that approximately 1,000 properties would be rehabilitated. The President of the DNDC in 2004 informed us that the DNDC staff lacked the expertise to accomplish the rehabilitation of the properties. The rehabilitation work completed was shoddy and mainly cosmetic, according to Ms. Warren. Ms. Warren informed us that, despite rental and sales revenue, the DNDC could not cover its expenses and the PDD decided to discontinue funding.

The attorney for the DNDC stated, "Since 2002, the goal of the DNDC has been to expeditiously dispose of the DNDC's interests in property in the City of Detroit. The disposition of such interests was undertaken with some sense of urgency because there is no independent revenue source to finance the operations of the DNDC, and the revenues generated by the sale of the DNDC's interests in properties were not sufficient to cover the ongoing operating costs of the DNDC, including the cost of salaries, rent and maintaining and insuring the properties. Since 2002, the DNDC has disposed of most of its interests in its portfolio and is now negotiating the sale of the remaining interests."



The middlemen sold 264 of the 373 homes for \$5.8 million or an average of \$22,118 per home. They flipped (sold within 21 days) 158 homes for \$1.5 million; 76 of which were resold on the same day they were acquired from the DNDC.

Table 1 reflects sales information, related to 74 purchases from the DNDC, for which we could determine the sales price paid to the DNDC.

**TABLE 1**

Middleman	Properties Purchased From DNDC	Amounts Paid to DNDC	Properties Sold by Middlemen	Total Amount From Sales*	Properties Flipped **	Flipped Sales Amounts	PDD Mortgage
Brown	7	\$ 1,206	4	\$ 6,500	4	\$ 6,500	
Shows	20	171,001	20	1,243,850	0	0	\$304,494
Jackson	17	30,802	17	735,200	1	15,000	
Turner	30	36,100	4	236,000	0	0	
Total	74	\$239,109	45	\$2,221,550	5	\$21,500	\$304,494

\* Total amount from sales includes flipped sales amounts.

\*\*Flips are properties purchased and sold within 21 days.

Quit Claim deeds reflect that the 74 homes were sold by the DNDC to the middlemen for \$239,109. The average price was \$3,231 per home. The middlemen sold 45 of the 74 homes that they had purchased for \$207,705 for \$2,221,550. This represents an increase of \$2,013,845 over the purchase price, and an average sales price of \$49,368 per home.

Table 2 reflects sales information for the remaining 299 properties purchased by the middlemen.

**TABLE 2**

Middleman	Properties Purchased From DNDC	Amounts Paid to DNDC	Properties Sold by Middlemen	Total Amount From Sales*	Properties Flipped**	Flipped Sales Amounts	PDD Mortgage
Brown	56	Unknown	55	\$ 254,003	55	\$254,003	
Shows	37	Unknown	24	773,057	16	371,401	\$334,370
Jackson	167	Unknown	115	2,060,195	79	839,010	
Turner	39	Unknown	25	530,462	3	12,400	
Total	299	Unknown	219	\$3,617,717	153	\$1,476,814	\$334,370

\* Total amount from sales includes flipped sales amounts but excludes PDD mortgage amounts.

\*\*Flips are properties purchased and sold within 21 days.

We could not determine the total amounts paid to the DNDC for these properties, because neither PDD or DNDC provided access to records, and tax valuation affidavits were filed for the sales, and the sales price was not disclosed. The middlemen sold 219 properties for \$3.6 million, an average of \$16,519 per property. The middlemen averaged \$9,652 on the 153 properties that were flipped, and \$32,438 on the 66 properties that were sold after 21 days.





In addition, we determined that:

- New Detroit Real Estate Management, LLC received another \$638,846 in income from 24 mortgages from the buyers who received mortgages from the PDD's homebuyer assistance program.
- Dalton Brown/Chayne Holding Group, LLC resold 41 properties on the same day, and 18 within 21 days of purchasing the property from the DNDC. Dalton Brown/Chayne Holding Group, LLC sold most of the properties for \$5,500 - \$6,500.

Based on the resale amount and the timing of the resale, it is clear that the DNDC could have increased the amount of revenue received on its sales and increased its ability to reimburse the City for the initial cash outlays used to purchase the properties.



### **In Summary,**

- The Office of the Auditor General noted the sale by the DNDC of 373 properties to four businesses or individuals identified above.
- 264 properties, which were sold to the four businesses or individuals, were ultimately sold for over \$5.8 million.
- The total received from the sales by DNDC cannot be determined because the City's Chief Development Office and the DNDC President have refused to provide documents related to the sales.
- Information about the DNDC property sales and vendor contracts is limited to a few individuals, without any independent oversight. Moreover, detailed information about the DNDC transactions has been withheld from the Auditor General.

### **We, therefore, recommend**

That the City Council use its resources to immediately issue a subpoena jointly, from the City Council and the Office of the Auditor General, for DNDC and PDD records and individuals. Records that should be subpoenaed include:

- DNDC's bank statements and cancelled checks for the period January 1, 2001 to September 30, 2005;
- Any and all DNDC records pertaining to all real estate sales occurring between the period January 1, 2001 and September 30, 2005;
- DNDC's accounting records for the period January 1, 2001 and September 30, 2005, including: payroll records, purchasing records, accounts receivable records, accounts payable records, inventory records, fixed asset records, cash receipts journals, check registers, general ledger records, and DNDC's Profit and Loss Statements and Balance Sheets;
- Vendor contracts entered into by DNDC during the period;
- Invoices for goods and services received by DNDC;
- Any and all records related to the rehabilitation of properties occurring between the period January 1, 2001 and September 30, 2005;
- Listing of DNDC employees and officers during the period January 1, 2001 to September 30, 2005;
- Records supporting PDD's payments to DNDC during the period January 1, 2001 to September 30, 2005;
- Records supporting PDD's receipts from DNDC during the period January 1, 2001 to September 30, 2005;
- DNDC's policies and procedures for selling and rehabilitating properties;
- DNDC's property inventory records for the period January 1, 2001 to September 30, 2005;





- DNDC's audit reports and tax returns;
- Lewis & Munday's letter on the inappropriate use of bond funds;
- List of rental properties; and
- Any and all other related documents pertaining to this matter.

Individuals that should be subpoenaed include:

- Mr. Walter Watkins;
- Ms. Jannie Warren;
- Mr. O'Neil Edwards;
- Ms. Sylvia Bradley;
- Ms. Tracey Robinson; and
- Any past or current PDD or DNDC employee or officer who has knowledge pertaining to this matter.